



Platinum
World Portfolios
Asia Fund

Quarterly Investment
Manager's Report

31 March 2016

Platinum World Portfolios - Asia Fund



Joseph Lai Portfolio Manager

Disposition of Fund Assets

| REGION | MAR 2016 | DEC 2015 |
|----------------------------|------------|------------|
| China (Listed Ex PRC) | 30% | 25% |
| China (Listed PRC) | 7% | 7% |
| Hong Kong | 4% | 3% |
| Taiwan | 4% | 3% |
| Greater China Total | 45% | 38% |
| India | 18% | 18% |
| Korea | 9% | 6% |
| Thailand | 7% | 3% |
| Philippines | 4% | 4% |
| Singapore | 3% | 2% |
| Vietnam | 2% | 0% |
| Cash | 12% | 29% |

Source: Platinum. Refer to note 2.

Performance

(compound pa, to 31 March 2016)

| | QUARTER | SINCE INCEPTION |
|---------------------------------|---------|-----------------|
| PWP - Asia Fund (Class D) | -1% | -1% |
| MSCI AC Asia ex Japan Net Index | 2% | 2% |

Source: Platinum and MSCI. Refer to note 1.

The Indian Nifty 50 Index was down -3% and the China's Shanghai A-Share Index returned -15% for the quarter (both in local currency). The Reserve Bank of India's (RBI) push to clean up bank balance sheets led to a significant increase in non-performing loans for many Indian banks, worsening market sentiments as a whole. The Chinese market was rocked by a volatile Yuan and the ill-conceived implementation of a "circuit-breaker" in the retail-driven mainland A-share market. However, a cleaner loan book and monetary loosening for India and evident economic stabilisation in China should lift the market outlook for these countries.

Markets in the ASEAN region were better performers. Thailand, Indonesia and Malaysia were respectively up +9%, +5% and +1% (each in local currency) for the quarter. These markets saw slower economic growth and had had their domestic monetary policy hamstrung by the US tightening last year. With the prospect of a brisk US interest rate hike receding, local currencies and stock markets came back to life.

As expected, the Fund's ASEAN holdings were contributors to performance. Jardine Matheson (ASEAN consumption conglomerate, +17%) and Bangkok Bank (+18%) (each in local currency) were strong performers. Elsewhere, Kweichow Moutai (Chinese liquor producer, +14%) and Yes Bank (Indian bank, +19%) (each in local currency) also contributed. Chinese and Indian financials (PICC, China Pacific Insurance and ICICI Bank) detracted from performance.

Changes to the Portfolio

The Fund's Chinese currency short position was kept open as continued policy stimulation out of China is likely to lead to renewed weakness, despite recent strengths. The Fund increased its invested position to 88%, taking advantage of weakness in the markets during the quarter.

We exited our position in US-listed **YY.com** after the company received a privatisation offer. Funds raised were deployed into more prospective ideas.

We started positions in **CNOOC** and **ENN Energy**, both of which are set to benefit from a recovery in oil prices. CNOOC is a major Chinese oil player which controls the bulk of oil reserves off the coast of China and has an enviable production profile. ENN is a Chinese downstream gas distributor with monopolies across numerous Chinese cities. The structural rise of incomes among China's middle class will drive energy consumption. The recent weakness in the market enabled us to add to these structurally strong companies at attractive valuations.

Commentary

India

We conducted a research trip to India in February, focusing on banking, infrastructure and real estate. We did not uncover any adverse surprises. India has an exceptionally young and aspirational population seeking jobs and a better life, and the authorities are responding.

On our trip we visited Yes Bank, currently the top Indian position in the Fund's portfolio. From a standing start just 10 years ago, Yes Bank has grown into the country's fifth largest private sector bank. The company boasts an excellent management team who understands the importance of risk management. During the quarter, the RBI examined the loan books of Indian banks to ensure that bad loans are recognised and dealt with promptly. The RBI's review showed that Yes Bank's asset quality was superior to even the most revered private sector banks in India, with a non-performing loan ratio of just 0.66% and no history of restructuring for five quarters. With just 1% market share in an industry still dominated by the inefficient state banks, the runway ahead for Yes Bank is tremendous.

Reforms are ongoing and progress is palpable throughout the country. Subsidies previously trapped by the middle-man are now increasingly disbursed directly into consumers' bank accounts, thanks to the implementation of the national ID system (Aadhaar), covering approximately one billion people. Government services are moving online, and with them a greater degree of transparency.

A key challenge for India is the lack of basic infrastructure. The shortage of reliable power supply puts major constraints on growth, but critical progress is taking place. Inadequate domestic coal supply had been a perennial problem. Against most pundits' expectations, however, coal production has lifted significantly in recent months, so much so that imports fell 15% year-on-year over April-December 2015!

India's power sector has also been plagued by a lack of accountability of state governments in managing the finances of state-owned electricity distribution companies. Artificially low tariffs for certain groups and outright theft in other cases have led to distribution companies racking up huge losses, impairing their ability to purchase power. To fix the problem, the central government put forward a reform proposal which aims to reduce the interest cost of distribution companies and make them more accountable to losses. Since our last update in the December 2015 Quarterly Report, another six states have in principle endorsed the scheme, taking the total number of participating states to 17. Nine of these 17 states have already signed a memorandum of understanding with the central government. These nine states had a combined debt of approximately US\$29 billion, representing 45% of the power distribution sector's total outstanding debt! We expect to see an improvement in power demand and NTPC, India's largest power utility and one of the Fund's top three positions in India, would be a key beneficiary.

While there remains a long way to go for infrastructure improvement, road building continues to pick up with the National Highways Authority of India and the Ministry of Road Transport and Highways together completing 3,980 km of highways during April to December 2015, averaging 14.5km per day, a significant increase from a year prior. We hope to take advantage of this trend through the Fund's holdings in IRB Infrastructure Developers, a leading road construction company and tollway operator.

Similarly, rail capital expenditure is also improving and investments in the Dedicated Freight Corridor will drive demand for container logistics. The recent central government budget showed that planned spending for railway will increase by 24% year-on-year. One of the Fund's key holdings, Adani Ports, has a third of the market share of private ports in India, is seeing a rapid rise in container traffic as a result of ongoing economic growth and increasing containerisation in freight transport.

Residential property sales across the top seven cities are now 20% lower from the 2013 peak after two consecutive years of decline. In March, the upper house of the Indian Parliament passed a real estate bill which proposes to regulate both commercial and residential sectors. The reforms are focused on increasing consumer protection through mandatory project registration requirements, introducing the use of escrow accounts (to ensure that funds are not used for other corporate purposes) and imposing penalties on developers for construction delays. All these measures, if implemented, will bring about positive changes to the sector and accelerate its transition from scattered players into an organised industry.

China

The beginning of the quarter was eventful in China. The implementation of a stock market circuit breaker on the first trading day of 2016 precipitated in a panic sell-off, with domestic punters concerned that a suspension would prevent them from selling their holdings. The policy intent was to reduce volatility, but it produced the opposite outcome. To the credit of the Chinese authorities, the measure was abolished within a week.

The Yuan depreciated 1% in the first week of the year. China runs a sizable trade surplus, which means money should naturally flow into the country via trade. However, the expectation of Yuan depreciation led to corporates paying down their US dollar debt and locals becoming eager to diversify their asset base offshore, which resulted in much downward pressure on the currency.

However, the immediate pressure to depreciate has reduced as repayment of foreign debt has begun to stabilise (it is estimated that some US\$300 billion, or 30% of Chinese companies' foreign debt, was repaid last year), and the Chinese authorities have stepped up their efforts to crack down on underground channels that facilitate capital outflow (including greater scrutiny on the practice of over-invoicing of imports). Moreover, expectations of further interest rate rises in the US have subsided. We would note, however, while the short-term pressure has lessened, longer-term pressure to gradually devalue the currency remains as China will need further monetary stimulation.

China's National People's Congress held its annual meeting in March. The conference held special significance this year, as it marked the beginning of China's 13th Five-Year Plan. The message, once again, emphasised the continuation of reform to restructure the economy towards greater consumer and service orientation. Key policies include:

- Encouraging consumption through increasing public spending on social welfare and healthcare.
- Trimming down excess capacity in old industries (e.g. steel and coal) to reduce "zombie companies" and reform state-owned enterprises (SOEs) to make them operate more like private businesses.
- Further urbanisation (currently around 56%) will be facilitated through modifying the *hukou* (household registration) system which has hitherto restricted the migration of labour (particularly from rural to urban areas).
- Strong emphasis on environmental protection, lifting emission standards and raising adoption rate of renewable energy.

China is a complex US\$10 trillion economy in which individual companies' prospects can differ enormously, depending on which part of the economy they operate in. China's previous growth story was predicated on encouraging its people to produce goods in the cities and save a large proportion of their money so that the banking system could deploy the savings into investments in infrastructure which in turn would lift productivity. Relying largely on domestically sourced savings to fund growth makes China unique among most developing countries and gives the authorities much flexibility when it comes to fiscal stimulus.

Policy stimulation over the last six months is leading to early signs of a cyclical recovery in the construction sector. Stabilisation was the key reason that sentiments towards commodities-related sectors have suddenly turned in recent months. New infrastructure project approval rate was up 40% this quarter. Property sales volume was up around 30% in the first two months of 2016. Pent-up demand for property proved so high that top tier cities (e.g. Shanghai and Shenzhen) had to tighten property purchase policies to keep prospective (investment) buyers in check! Even the smaller cities are seeing rapid recovery in investor interest, but it will take some time for sales strength to clear property inventory in these problematic smaller cities with a large number of unsold apartments.

One key driver for China's economic transition is to encourage consumption rather than savings. During the last 30 years of the *Chinese economic miracle*, household consumption as a percentage to GDP in fact declined from 50% to less than 40% today. An upshift of the portion of income consumed versus that saved will result in the biggest group of growing consumers the world has ever seen! Old economy-based

industries will see a long-term decline while new industries will grow. The transition will mean concomitant job losses and gains as well as slower economic growth, punctuated by bouts of policy stimulation.

Our investment in China is focused on longer-term growth of businesses that will do well as the country transitions into a consumer-oriented economy. Chinese consumer preferences are rapidly evolving. They are moving online quicker than ever, are becoming more discerning when it comes to product quality, and are increasingly attuned to leisure and health related consumption. To capture the opportunities created by these evolving consumption trends, the Fund has exposures to Internet companies (Tencent, JD.com, Baidu, Sina), insurance providers (China Pacific, PICC, China Taiping), premium branded liquor makers (Kweichow Moutai, Jiangsu Yanghe Brewery), gas utilities (China Resources Gas, ENN Energy), dominant domestic sporting brand (Anta Sports) and telecommunications (China Mobile). We are confident that these companies will grow to be much bigger businesses in China's new economic landscape.

ASEAN

Outside of India and China, the Fund also has exposure to a range of high quality companies in the ASEAN region. In the Philippines, our key exposure is Ayala Land, the premier property developer with a vast land bank in this demographically young and populous country which is currently enjoying blistering economic growth and rising incomes. Jardine Matheson is a conglomerate with decades of experience operating in Asia and has enviably strong businesses in car assembly (one out of every two cars sold in Indonesia is made by its associate company Astra), retailing (Dairy Farm), office leasing (being the landlord of a significant part of Hong Kong's CBD), and hotel operation (Mandarin Oriental). In Thailand, we have positions in the major banks, Kasikornbank and Bangkok Bank, both of which will benefit from the country's long-term development. In Vietnam, the Fund holds a sizable position in the country's dominant dairy company. Vietnam is a populous country and its economic growth has recently been a bright spot in a lacklustre world. Post its joining the World Trade Organisation in 2007, Vietnam's export sector has been growing at double digit rates and household income has been rapidly rising.

Outlook

Recent events remind us that while one should not expect a linear growth trajectory, both China and India are gradually reforming to better their longer-term outcomes. This is beneficial to strong businesses in the more prospective industries.

Power sector reforms and a clean-up of non-performing loans are transformational steps for India. Sensible central government policies have reined in inflationary pressures, opening the way for interest rate cuts. In China, not only are reform efforts progressing, activities in the property market and infrastructure spending have both found a more stable footing. The ASEAN countries continue to develop as their predominantly young population join the workforce, start a business and become consumers in their own right.

Market weakness is presenting us with new opportunities. A low starting valuation reduces the risk of overpaying and increases the likelihood of positive returns. We remain optimistic as we find prospective companies to deploy the Fund's capital.

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An umbrella fund with segregated liability between sub-funds
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Notes

1. The Fund's total returns are calculated using its net asset value attributable to the relevant share class (where applicable) and represent its combined income and capital returns for the specified period. The Fund's total returns are pre-tax and are net of fees and expenses (excluding investment performance fees, if any). The Fund's returns are historical only. Past performance is not a reliable indicator of future performance and no warranty can be given or is given for future performance of the Fund. Owing to the volatility of the underlying assets of the Fund and other risks associated with investing, investment returns can be negative (particularly in the short-term). Investment returns and share prices fluctuate with market conditions, and investors may have a gain or loss when shares are sold. Fund performance changes over time and the return as of the time of your access to the information presented herein may be significantly lower than the historical returns stated above. The index represented is the MSCI All Country Asia ex Japan Net Index (US\$) (the "Index"). Index data has been sourced from MSCI Inc. Index returns include dividends but, unlike the Fund's returns, do not reflect fees or expenses. It should be noted that the Investment Manager does not invest by reference to the weighting of the Index. Underlying assets of the Fund are chosen through the Investment Manager's individual stock selection process and as a result holdings vary considerably to the make-up of the Index. The Index is provided as a reference only.

The inception date for Class D of the Fund is 16 November 2015. The inception date for the purpose of calculating Index returns, as contained in this publication, is taken to be the inception date of Class D of the Fund.

2. Invested position represents the exposure of physical holdings and long stock derivatives.

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